Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	CC Docket No. 98-121
Application of BellSouth Corporation,	)	
BellSouth Telecommunications, Inc.	)	
and BellSouth Long Distance, Inc.	)	
for Provision of In-Region, InterLATA	)	
Services in Louisiana	)	

Exhibit AA:
Application of BellSouth BSE, Inc. for Authority to Provide Local Exchange Service,
Kentucky PSC Case No. 97-417 (June 8, 1998)

THE COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF BELLSOUTH BSE, INC. FOR AUTHORITY TO PROVIDE LOCAL EXCHANGE SERVICE	)))	CASE NO. 97-417

ORDER

INTRODUCTION

On October 1, 1997, BellSouth BSE, Inc. ("BSE") filed its application with the Kentucky Public Service Commission for approval to provide local exchange service in Kentucky. BSE is a wholly owned subsidiary of BellSouth BSE Holdings, Inc. which in turn is a wholly owned subsidiary of BellSouth Corporation ("BellSouth"). BellSouth Telecommunications, Inc. ("BST") is the largest incumbent local exchange carrier ("ILEC") in Kentucky and is also a wholly owned subsidiary of BellSouth. In connection with this application, BSE and BST have submitted their interconnection agreement for approval pursuant to 47 U.S.C. § 252(e).

AT&T Communications of the South Central States, Inc. ("AT&T"), the Southeastern Competitive Carriers Association ("SECCA"), MCI Telecommunications Corporation and MCImetro Access Transmission Services Inc. ("MCI"), and the Kentucky CATV Association, Inc., d/b/a Kentucky Cable Telecommunications Association ("KCTA") intervened. The Intervenors claim, among other things, that provision of local exchange service by BSE in BST territory would have anti-competitive effects, enabling BellSouth to avoid the legal restrictions imposed on BST as an ILEC. The Intervenors also claim that

BSE services, subsidized by BST by means of less than arm's-length transactions, would be priced below cost and would force legitimate competitors out of the market. On April 24, 1998, the Commission conducted a hearing on the matter, and subsequently BSE, AT&T, and SECCA and MCI jointly, submitted briefs.

CERTIFICATION REQUIREMENTS

BSE contends that its application meets the Commission's requirements for certification as a competitive local exchange carrier ("CLEC"). BSE asserts it has demonstrated to the Commission that it has the technical, managerial, and financial abilities to provide adequate service pursuant to KRS 278.020; it has submitted an interconnection agreement, 47 U.S.C. § 252; and it has submitted a local service tariff pursuant to KRS 278.160.[1]

The Intervenors herein contend that BSE lacks the financial resources to operate as a CLEC because it must depend upon the resources of its parent company. As BSE points out,[2] the Commission has certified other CLEC applicants that initially relied upon the resources of their parent companies. AT&T argues that BSE also lacks technical and managerial resources and depends upon the experience and expertise of employees of its affiliates.

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[1] Post Hearing Brief of BellSouth BSE, Inc., filed May 26, 1998 ("BSE Brief"), at 1-2.

[2] BSE Brief at 2.

In Administrative Case No. 370,[3] pursuant to its authority under KRS 278.512 to exempt certain telecommunications carriers and products from statutory and regulatory requirements, the Commission determined that requiring CLECs to file applications to begin operations is no longer necessary to protect the public. CLECs, as such, possess neither market power nor own local exchange bottleneck facilities; moreover, there is no need for the Commission to monitor their financial stability to ensure their continued existence, since financial failure of a CLEC would not deprive customers of their carrier of last resort.[4] Accordingly, BSE is technically correct: its filings at the Commission are sufficient, pursuant to current regulatory requirements for CLECs, to enable it to begin operations in Kentucky. However, as the Intervenors point out, BSE is not merely a CLEC. It is an affiliate of BST, Kentucky's largest incumbent local exchange carrier, and the evidence demonstrates that its operations are intricately intertwined with those of this powerful affiliate. It is the alleged potential for anti-competitive behavior and distortion of the competitive local exchange market that are the problematic issues here.

Thus, while the dependence of BSE on its parent is not technically relevant to certification per se, the close relationship between BSE and BST does raise concerns regarding the operational separation of the entities and the resulting potential for gaining an unfair pricing advantage. If BSE acquires services at a discount from BST and those services are delivered in the same manner as if the transaction never occurred, then it

[3] Administrative Case No. 370, Exemptions for Providers of Local Exchange Service Other Than Incumbent Local Exchange Carriers, Order dated January 8, 1998 ("Administrative Case 370 Order").

[4] Administrative Case 370 Order, at 2.

appears that overhead expenses associated with providing service incurred by a typical CLEC may never be realized by BSE. The conceptual framework for the development of competition and the incentives to operate more efficiently and reduce costs could thereby be negated by a variant of price arbitrage.

INCONSISTENCY WITH THE PURPOSES OF THE TELECOMMUNICATIONS ACT OF 1996

The Intervenors argue that, if BSE provides service in BST territory, BST could subsidize BSE's prices, enabling BSE to provide BST services on a retail basis at rates that neither earn a profit nor cover BSE's costs. The resulting price squeeze would force other CLECs, which will need to make a profit to survive, out of the market. AT&T contends that Congress foresaw that an ILEC might attempt to be a CLEC as well as an ILEC and therefore enacted 47 U.S.C. § 251(h), which provides that, when a comparable carrier substantially replaces an ILEC in its market, the obligations placed on an ILEC by the Telecommunications Act of 1996, Pub. L. No. 104-104,110 Stat. 56 (1996) (the "Act") must apply.[5] MCI and SECCA state that, in fact, to consider BSE a CLEC in areas served by BST would be to "ignore the only reasonable definition of a CLEC -- a local exchange carrier that competes against the entrenched incumbent for customers."[6] BSE, the Intervenors contend, would not actually "compete" with the incumbent BST. MCI and SECCA point out that, in hearings on BSE certification in South Carolina, BSE witness

[5] AT&T Brief at 11.

[6] SECCA and MCI Brief at 1.

Robert C. Scheye stated outright that BSE does not "really want to compete with BST."[7] The Intervenors not only claim that there is no real distinction between BST and BSE; they also argue that the public will perceive no difference between BSE and BST. Both carry the name "BellSouth" and will use the BellSouth logo.

The real purpose of BSE's existence, the Intervenors claim, is to enable BellSouth to provide local exchange services absent the restrictions placed upon it by the Act as an ILEC in possession of bottleneck facilities. BSE will, for example, not be required to make retail services available for resale to CLECs at wholesale rates pursuant to Section 251(c)(3) and (4) of the Act.

BSE argues, among other things, that allegations regarding potential anti-competitive behavior on its part are only "conjecture,"[8] and that there are adequate remedies to deal with such activities if they occur.[9] BSE also contends it would be economically irrational to operate in a less than profitable manner.[10] The latter argument, however, does not take into account the ultimate benefit to BellSouth of eliminating competitors from the local market; and while it is true that anti-competitive behavior of the nature predicted by the Intervenors has not yet occurred, the Commission finds that the

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[7] SECCA and MCI Brief at 3, citing Tr. 17, Before the South Carolina Public Service Commission, BellSouth BSE Application for a Certificate of Public Convenience and Necessity to Provide Local Exchange Telecommunications Services, Nov. 5, 1997, Docket No. 97-361-C.

[8] BSE Brief at 3.

[9] BSE Brief at 4.

[10] BSE Brief at 7, 8.

potential for such behavior would be greatly exacerbated by granting BSE the authority it seeks. Further, although remedies for violation of federal law do, of course, exist, this Commission does not routinely oversee the business activities of CLECs for the very reason that they do not possess the market power of an ILEC such as BellSouth.

CONCLUSIONS

The Commission regulates telecommunications services in the public interest. See, e.g., KRS 278.512(1)(c) ("[t]he public interest requires that the Public Service Commission . . . regulate and control the provision of telecommunications services to the public in a changing environment, giving due regard to the interests of consumers, the public, the providers of the telecommunications services, and the continued availability of good telecommunications service"). Public interest determinations "require consideration of all important consequences including anti-competitive effects." Denver & Rio Grande W.R.R. v. United States, 387 U.S. 485, 492 (1967). See also FCC v. RCA Communications, Inc., 346 U.S. 86, 94 (1953) ("There can be no doubt that competition is a relevant factor in weighing the public interest"). Section 252(e)(2)(A)(ii) of the Act provides that a state commission may reject an interconnection agreement on the ground that its implementation would not be "consistent with the public interest, convenience, and necessity."

The Commission finds that the public interest concerns raised by the Intervenors herein are grave ones justifying rejection of the BST/BSE interconnection agreement and denial, in part, of BSE's application to provide local exchange services in Kentucky.

IT IS THEREFORE ORDERED that:

1. BSE is granted the authority to provide intrastate telecommunications services as described in its application but only in areas outside the franchised service territory of BST.

2. The interconnection agreement between BSE and BST is rejected.

3. BSE shall incorporate the restriction on its service area in its tariff.

Done at Frankfort, Kentucky, this 8th day of June, 1998.

By the Commission

ATTEST:

Helen C. Helton

Executive Director

BB

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Exhibit BB:
<u>Application of BellSouth BSE, Inc. for a Certificate of Public Convenience and Necessity to Provide Local Exchange and Exchange Access Service as a Competing Local Provider in North Carolina</u>,
North Carolina PUC Docket No. P-691 (April 24, 1998)

STATE OF NORTH CAROLINA
UTILITIES COMMISSION
RALEIGH

DOCKET NO. P-691

BEFORE THE NORTH CAROLINA UTILITIES COMMISSION

In the Matter of		
Application of BellSouth BSE, Inc., for a Certificate of Public Convenience and Necessity to Provide Local Exchange and Exchange Access Service as a Competing Local Provider in North Carolina	)))))	ORDER RULING ON NEW ENTRANT'S SECOND DATA REQUEST

BY THE CHAIR: On March 16, 1998, the New Entrants, consisting of KMC Telecom Group, TCG of the Carolinas Inc., ICG Telecom Group, Inc., Interpath Communications, Inc., and DeltaCom, Inc., submitted a second set of data requests to BellSouth BSE (BSE) consisting of 9 questions numbered 30 through 39.

On March 23, 1998, BSE filed objections to these data requests as follows:

31	Proprietary, irrelevant
32	Same; no consultant studies
33	Proprietary, irrelevant
34	Same
36	Same

The Items read as follows:

31. State what assumptions were used in formulating said Income Statement. Alternatively, a copy of those assumptions may be produced.

32. Produce copies of all consultants' studies concerning BSE, its formation, its purposes and/or plans.

33. Produce copies of all BellSouth studies concerning BSE, its formation, its purposes and/or plans.

34. Produce copies of all BSE's marketing plans, which were formulated internally or produced by a consultant.

36. State by category (such as salaries, rent, and the like) the funds expended by BSE in 1997. Alternatively, an income and expense statement may be produced.

With respect to relevancy, BSE maintained that the relevant issues in this docket are whether:

1. BSE is fit, capable and financially able to render local service;

2. The services to be provided will meet Commission standards.

3 The provision of services by BSE will not adversely affect the availability of reasonably affordable local service;

4. BSE will participate in the support of universal service to the extent required; and

5. The provision of local service will not otherwise adversely impact the public interest.

BSE maintained that the New Entrants are seeking information concerning the current, medium and long-range business activities, strategies, and plans of BSE--an anticipated competitor to them--and such information is not relevant to the above statutory standards for certification.

On March 27, 1998, the New Entrants filed their Responses to BSE's Objections. The New Entrants noted that BSE had not objected to a First Set of Data Requests consisting of 30 questions. The New Entrants also had taken the depositions of two BSE employees in Atlanta but no objections as to confidentiality or relevance had been lodged concerning these depositions. However, because the witnesses had been unable to answer certain questions, the New Entrants filed the Second Set of Data Requests.

Concerning specific items objected to, the New Entrants replied as follows:

31	Income statement is part of application. New Entrants want assumptions or a copy of those assumptions. Directly relevant.
32	Directly relevant. However, if there are no consultant studies, this item is moot.
33	Directly relevant.
34	Directly relevant. Will sign confidentiality agreement.
36	Directly relevant to inquire as to what business BSE had undertaken to date, its resources, and how it has spent its funds.

On April 3, 1998, BSE filed a Reply to New Entrants' Response to BSE's Objections as follows:

31	BSE purports that New Entrants have limited their request as to "whether existing customers or contracts will migrate to BSE from BellSouth Telecommunications, whether customer referrals will be made or the like" and provided an answer on that basis.
32	BSE purports that the New Entrants have limited their request to "any more specific plans and, if so, whether those plans are anticompetitive in nature" and stated that it has already provided an answer. BSE reasserted its objection to providing any actual studies.
33	BSE purports that the New Entrants have limited their request to "internal BSE studies" as to "how" a new venture will operate," and contended that it has already responded.
34	BSE believes that it has already responded but reasserted its objection to providing any actual studies.
36	BSE purports that the New Entrants have clarified that they desire "what business BSE has undertaken to date, what its resources are, and how it spent its funds" and that BSE has already responded.

BSE also provided responses to Items 30, 35, 37, 38, and 39 in its Reply.

On April 8, 1998, the New Entrants filed a Motion to Compel Discovery. The New Entrants charged that BSE had erroneously stated that the New Entrants had narrowed the information sought in their data requests. The New Entrants also noted that they were willing to agree to a protective order that would have allowed only counsel for the New Entrants to review the information produced, but no further communication has been received from BSE. In its Motion to Compel, the New Entrants argued the following:

31	Relevant because they show how BSE plans to generate much business in a little time. Bear on issue of whether BSE's application is anticompetitive in nature.

32	Specific plans are necessary to assess whether those plans are anticompetitive. Willing to sign protective agreement.
33	Studies relevant to BSE's plans and whether anticompetitive. Willing to sign protective agreement.
34	BSE's projected growth rate makes it hard to understand how there could not be connections between BellSouth and BSE, which could be anticompetitive.
36	Expenditure information shows nature of business and whether substantial amounts have been spent on consultant studies.

Accordingly, BSE requested that BSE be compelled to respond to the above data requests fully and accurately. BSE further requested that the Commission the costs of this motion, including attorney's fees, against BSE.

On April 14, 1998, BSE faxed a letter to Mr. Daniel Long, Assistant Commission Attorney, and copied to the New Entrants which indicated the following:

31	BSE is preparing a summary of assumptions used in formulating its income statement and will forward a copy to New Entrants. Should resolve the dispute.
32	BSE stated that are no consultants' studies concerning BSE. Question is moot.
33	BSE stated that there are no BellSouth studies concerning BSE. Question is moot.
36	BSE is breaking down into major expense categories its 1997 expenses. Should resolve dispute

However, with respect to Item 34, BSE stated that it and the New Entrants have reached an impasse concerning the production of a consultant's study relative to BSE's marketing plans and strategies. The impasse concerns the location of production and the terms under which the New Entrants' counsel can copy needed portions of the consultant study. BSE's proposal is that the consultant study should be available for review by New Entrants' counsel at the Raleigh offices of Kilpatrick Stockton. New Entrants counsel may mark for copying those parts of the consultant study pertinent to its investigation of any potential anti-competitive effect of BSE's proposed activities. BSE would copy those portions and provide them to New Entrants' counsel within 24 hours. BSE characterized the New Entrants' position as being that BSE should release a complete copy of the consultant study to the custody and control of New Entrants' counsel for a period of seven to ten days whereupon portions of the consultant study not deemed pertinent to the inquiry would be returned to BSE. New Entrants' counsel would identify those portions of the consultant study he planned to use during the hearing within a week to ten days prior to the hearing.

BSE is not amenable to New Entrants' proposal. BSE believes the consultant study to be highly confidential and that it has offered reasonable accommodation to the New Entrants for access to the information.

On April 15, 1998, the New Entrants delivered a letter to Mr. Daniel Long and Ms. Mary Steel concerning the confidentiality dispute. The New Entrants stated that they favored a protective agreement similar to the one concluded with BellSouth in Docket No. P-100, Sub 133d. Those materials were also highly confidential but BellSouth was willing to produce a full copy of the confidential materials to New Entrants' counsel. The parties were able to use the confidential information at the hearing in a way that was not disruptive.

The New Entrants maintained that BSE's position on this matter has been and continues to be unreasonable. At first, BSE demanded that counsel for the New Entrants travel to Atlanta to review a copy of the study. He could take notes but would not be allowed to make copies. Later, BSE said that it would provide a copy of the study in Raleigh and copies could be made of portions of that study. The New Entrants argue that there is simply no reason not to provide a full copy of the study at their own offices for review. The New Entrants also identified what it called unacceptable provisions to the protective agreement BSE has proposed which, it contends, are either not true, require burdensome procedures, or purport to tell the Commission how to run its hearings.

On April 20, 1998, the New Entrants advised Mr. Long by telephone that BSE's responses to Items 31 and 36 were satisfactory. Since Items 32 and 33 are moot, this left as the sole issue the mode in which confidential information will be provided concerning Item 34.

Whereupon the Chair reaches the following

CONCLUSIONS

While the Chair appreciates the sensitivity with which BSE views the consultant's study requested in Item 34, the Chair also views the conditions that BSE has requested for New Entrant access to that information to be excessively burdensome. Parties have already agreed that only the New Entrant's counsel would have access to this information.

The fundamental logistical question remaining is whether BSE retains custody and control and New Entrants' attorney must view the materials at the Raleigh offices of BSE's counsel. The more fundamental question is whether it would be more appropriate to allow the New Entrants' counsel to view the materials outside of such confinement.

The Chair believes that New Entrants' counsel should be able to view and copy the materials outside of the confinement proposed by BSE. The Chair therefore concludes that the parties enter into a protective agreement along the lines of the terms previously used by BellSouth in Docket No. P-100, Sub 133d, as reasonably modified to fit the circumstances of this case. The New Entrant's are, of course, expected to take the utmost care that the subject material not be seen or read by unauthorized persons and to strictly abide by the protective agreement.

IT IS, THEREFORE, ORDERED that BSE and the New Entrant's enter into a protective agreement as stated above such that the New Entrant's counsel receives the information requested within 10 days of the issuance of this Order.

ISSUED BY ORDER OF THE CHAIR.

This the 24th day of April, 1998.

NORTH CAROLINA UTILITIES COMMISSION

Gail L. Mount

Gail L. Mount, Deputy Clerk

mz042498.02

cc

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Exhibit CC:
Merrill Lynch, "The Business Line Migration Phenomenon: The Numbers Don't Lie, ILEC Line Growth Remains Robust" (June 12, 1998)

Merrill Lynch

In-depth Report

United States
Telecommunications/Services

12 June 1998

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Telecom Services — Local

The Business Line Migration Phenomenon: The Numbers Don't Lie, ILEC Line Growth Remains Robust

Reason for Report: Analysis of Local Access Line Growth

Industry

Highlights:

- **We have reanalyzed first quarter's line additions and line growth statistics; adjusting lines to an access line equivalent ("ALE") basis so that the data at the ILECs and the CLECs is consistent and so that it more accurately reflects the capacity being used by customers.**
- **Despite the slowdown in the RBOCs' reported switched business line additions in 1Q98, our analysis suggests that the group's business line growth remains strong when high-speed lines, measured on an access line equivalent basis consistent with the CLECs, are included. Traditional measures reported by the RBOCs do not reflect the business line migration phenomenon, because they only count single business (or POTs) lines.**
- **By including DS-1s and DS-3s in ILEC access line equivalent counts, we have not only captured the business line migration phenomenon, but also discovered the overall local telecom market is growing at a rate in which both newer entrants and the incumbents can benefit. The CLECs continue to take share at a steady clip at the same time as the RBOCs and independent telcos have sustained line additions. The pie is getting bigger; thank you Internet, AOL, ISPs, fax machines, computer modems, etc.**
- **The industry added almost 3.4M local ALEs in 1Q, an increase from 4Q97's 2.9M ALE additions and 1Q97's 2.8M adds. Of the industry's total ALE additions, the incumbent local exchange carriers' (ILECs) captured 2.8M lines comprising 82.7% of the total additions (vs. 81.8% in 4Q97 and 93.5% in 1Q97). CLECs and LD companies captured only 17% of total ALE additions.**
- **For business lines alone, the ILECs added more business ALEs in 1Q than in previous quarters. The ILECs added approximately 1.3M business ALEs in 1Q98 (or 69.5% of net additions), greater than the 1.2M reported in 4Q97 and in line with the year-ago quarter. CLEC and long distance companies captured 30% of the business ALE additions – much less than the 50+% suggested by a cursory look.**
- **As a result of the ballooning "need for speed," we believe there is a migration of business customers trading up their single POTs lines for high-speed (as well as higher rate) data lines. We estimate high-speed data lines have grown 25-35% y/y.**

Merrill Lynch & Co.
Global Securities Research & Economics Group
Global Fundamental Equity Research Department

435200/435100/435000 RC#60216306

The Numbers Don't Lie — Line Growth Remains Robust for the Entire Sector

■ What We Did:

The RBOCs' reported access line figures ignore high speed/high-bandwidth lines.

We have recalculated access line growth statistics for the RBOCs by including high-speed lines, attempting to put the group on a comparable basis with the CLECs' line count methodology. The RBOCs' reported line statistics ignore an increasingly important component of the RBOC growth story — the rapid growth of higher-speed/higher-priced/higher-bandwidth business lines (e.g., DS1s, DS3s, and, for the most part, ISDN lines). **When high-speed lines are converted to access line equivalents ("ALEs"), the numbers tell a much different story than has been reported.** We have used conversion multipliers as follows:

Table 1: Access Line Equivalent (ALE) Conversion Factors

Line Type	# Access Line Equivalents (ALEs)
POTs/DSO (Single Lines)	1
Basic Rate (BRI) ISDN	2
Primary Rate (PRI) ISDN	23
DS1/T-1	2.5
DS3 (= 28 DS1s or 28 x 2.5=70)	70

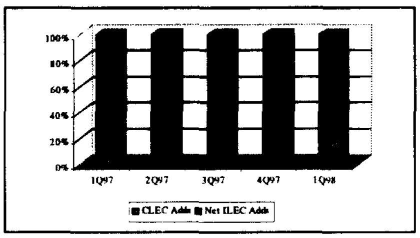
Source: Merrill Lynch estimates

■ What We Found:

The industry added almost 3.4M business and residential line equivalents in 1Q, more than ever before. 83% were captured by the ILECs & 17% by CLECs.

The local industry added almost 3.4 million business and residential local access line equivalents in the first quarter, an increase from 4Q97's 2.9 million ALE additions and 1Q97's 2.8 million adds. Of the industry's total ALE additions in the first quarter, the incumbent local exchange carriers' (ILECs) captured 2.8 million lines comprising 83% of the total additions (vs. 82% in 4Q97 and 93.5% in 1Q97). Despite the CLECs' strong growth — adding 580,000 lines in the first quarter — the group made up only 17% of total ALE additions (down slightly from 18% in 4Q97, but up dramatically from 1Q97's 6.5%) *(See Chart 1 & Table 2).*

Chart 1: % of Total ALE Adds



Source: Company reports, Merrill Lynch estimates.

Table 2: Total Access Line Equivalent Net Additions

	1Q97	2Q97	3Q97	4Q97	1Q98
New Entrant Adds [1]	180,000	251,189	420,194	522,148	579,922
% of Total Adds	***6.5%***	***11.5%***	***14.2%***	***18.2%***	***17.3%***
Gross RBOC Line Adds	2,135,757	1,643,180	2,196,518	2,057,926	2,428,251
Gross Independent Line Adds [2]	498,733	374,753	503,138	479,423	568,549
Total Gross ILEC Line Adds	2,634,491	2,017,933	2,699,657	2,537,349	2,996,800
Less: Estimated TSR Lines [3]	(63,000)	(87,900)	(151,270)	(193,195)	(220,163)
Net ILEC Adds [3]	2,571,491	1,930,034	2,548,387	2,344,154	2,776,429
% of Total Adds	***93.5 %***	***88.5%***	***85.8%***	***81.8%***	***82.7%***
Total Line Adds	2,751,491	2,181,223	2,968,581	2,866,302	3,356,351

[1] Includes CLEC and long distance company local line adds.
[2] Assumes Independent lines encompass 20% of total U.S. ILEC lines.
[3] TSR = Total Service Resale.
ILEC line counts have been reduced to account for TSR lines, which are double-counted.
Source: Company reports, Merrill Lynch estimates.

Table 3: Access Line Gains by New Entrants

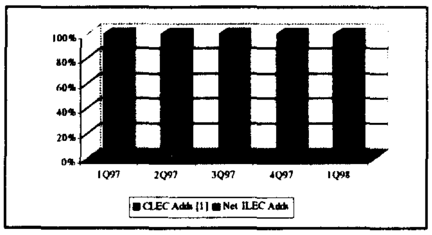
Line Additions	1Q97	2Q97	3Q97	4Q97	1Q98	2Q98E	3Q98E	4Q98E	1998E
CLECs		229,189	383,694	471,148	512,422	582,965	669,000	782,000	2,545,840
LD Companies [1]		22,000	36,500	51,000	67,500	78,100	88,900	99,800	334,300
Total Line Adds [2]	**180,000**	**251,189**	**420,194**	**522,148**	**579,922**	**661,065**	**757,900**	**881,800**	**2,880,140**
Sequential Growth			*67%*	*24%*	*11%*	*14%*	*15%*	*16%*	
Est. Total US Access Lines (Mils) [3]	167	168	169	170	172	173	175	176	177
% of Total US Line (gained in qtr.)	***0.11%***	***0.15%***	***0.26%***	***0.31%***	***0.34%***	***0.38%***	***0.43%***	***0.50%***	-
CLEC Annualized Share Gain (of Lines)		***0.6%***	***1.0%***	***1.2%***	***1.4%***	***1.5%***	***1.7%***	***2.0%***	***1.6%***

[1] AT&T, Sprint and MCI local line additions are Merrill Lynch estimates.
[2] Based on reported access lines. Net of lines acquired via merger or acquisition.
[3] Based on reported access lines. Access line equivalent figures would be greater.

CLEC line adds amounted to only 30.5% of industry-wide business ALE adds.

As shown in Table 3, the CLECs (including the long distance companies) added almost 580,000 line equivalents during the first quarter, up from 522,000 in 4Q97 and an estimated 180,000 lines in 1Q97. We deducted total resale lines (TSR) from the incumbent local exchange carriers' (ILECs) line counts — as they are double counted in the CLECs' line figures. Of the 3.4 million industry-wide ALEs added during the first quarter, 1.9 million were business ALEs. Of these, **the ILECs (including GTE and the other independent telcos) captured approximately 1.3 million business ALEs (or 69.5% of net additions), in line with the year ago quarter's additions.** With 580,000 access line adds, the CLECs captured only 30.5% of the total U.S. business ALE growth in the first quarter, up significantly from an estimated 11.8% in 1Q97 and 30.2% in 4Q97. Clearly, the CLEC have not yet captured anywhere near the 50% of net industry growth reported by some *(see Table 4 & Chart 2).*

Chart 2: % Business ALE Adds



[1] Assumes all CLEC lines are business lines. ILEC ALEs are net of lines resold by competitors.
Source: Company reports, Merrill Lynch estimates

Table 4: Business Access Line Equivalent Net Additions

	1Q97	2Q97	3Q97	4Q97	1Q98
CLEC Adds [1]	180,000	251,189	420,194	522,148	579,922
% of Total Adds	***11.8%***	***15.6%***	***21.3%***	***30.2%***	***30.5%***
Gross RBOC Line Adds [2]	1,154,757	1,182,180	1,508,518	1,149,926	1,263,251
Gross Independent Line Adds [2] [3]	253,483	259,503	331,138	252,423	277,299
Total Gross ILEC Line Adds [2]	1,408,241	1,441,683	1,839,657	1,402,349	1,540,550
Less: TSR Lines [4]	(63,000)	(87,916)	(155,400)	(193,195)	(220,163)
Net ILEC Adds [4]	1,345,241	1,353,767	1,684,256	1,209,154	1,320,387
% of Total Adds	***88.2%***	***84.4%***	***78.6%***	***69.8%***	***69.5%***
Total Net Business Line Adds	1,475,538	1,604,956	2,104,450	1,731,302	1,900,309

[1] Assumes all CLEC adds are business lines.
[2] "Gross" is net of churn but before deduction of TSR lines.
[3] Assumes Independents encompass 18% of ILEC business lines.
[4] ILEC line counts have been reduced to account for TSR lines, which are double-counted in CLECs' line statistics.

RBOC business line equivalents net adds remain strong, growing 10.1% y/y in 1Q98 and adding more new ALEs than ever before despite increased losses to competition.

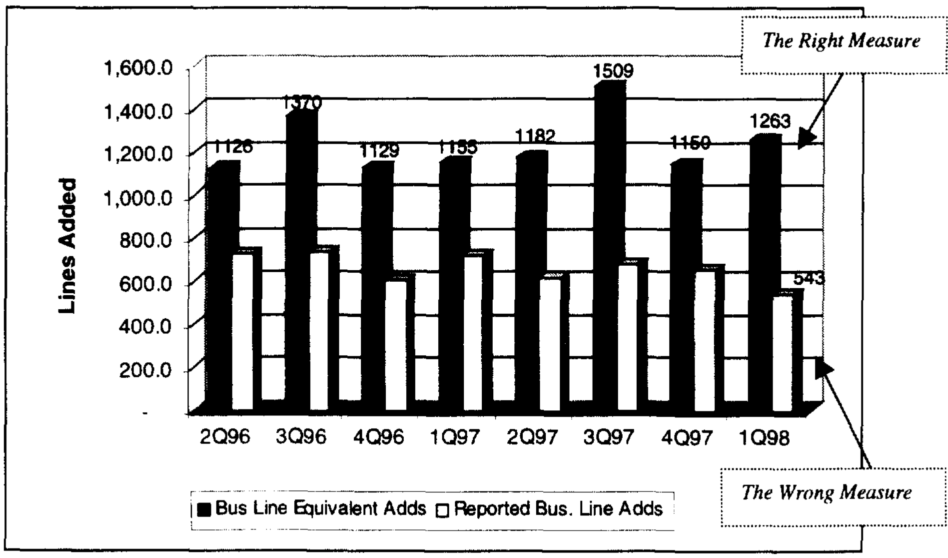
Finally, the RBOCs added more business line equivalents in the first quarter than the year-ago first quarter and the same holds true for previous quarters. The RBOCs added almost 1.3 million business ALEs (before deducting TSR lines) in 1Q98, 9.5% more than the 1.2 million adds in both 4Q97 and the year-ago quarter *(see Chart 3 and Table 5).* During 1Q98, the RBOCs' business access line equivalents grew 10.1% y/y, in line with 4Q's growth rate and only a modest deceleration from 1Q97's 10.4% rise.

Table 5: RBOC Business Access Line Equivalent Growth [1]

Totals*:	1Q96	2Q96	3Q96	4Q96	1Q97	2Q97	3Q97	4Q97	1Q98
Line Equivalents in Service [2]:									
POTS/DS0	41,513	42,197	42,868	43,381	43,959	44,471	44,979	45,393	45,759
ISDN	1,322.2	1,537.7	1,813.3	2,136.5	2,450.0	2,792.8	3,143.5	3,525.4	4,000.9
DS1	1,184.9	1,280.8	1,385.6	1,510.7	1,642.3	1,767.5	1,928.9	2,076.4	2,211.8
DS3	1,825.8	1,957.2	2,275.3	2,443.1	2,574.6	2,776.8	3,265.1	3,472.4	3,758.3
Total Business ALEs	**45,846.0**	**46,972.5**	**48,342.0**	**49,471.4**	**50,626.2**	**51,808.4**	**53,316.9**	**54,466.8**	**55,730.1**
y/y Growth					***10.4%***	***10.3%***	***10.3%***	***10.1%***	***10.1%***
Business ALE Additions		***1,126.5***	***1,369.5***	***1,129.4***	***1,154.8***	***1,182.2***	***1,508.5***	***1,149.9***	***1,263.3***

[1] Net residential additions. Before TSR lines are subtracted. RBOCs recover (in wholesale receipts) approximately 80% of revenue lost to CLECs using TSR.
[2] Line equivalents are equated as follows: 1 Basic rate ISDN trunk = 2 lines; 1 Primary Rate ISDN = 23 lines; 1 DS1 trunk = 2.5 lines; 1 DS3 trunk = 70 lines (28 DSIS or 28 x 2.5)
Source: Data for Bell Atlantic, BellSouth, SBC & U S WEST supplied by companies. Ameritech's lines have been estimated on a proportional basis.
*See Tables 8-12 for detailed calculations.

Chart 3: RBOC Gross ALE Adds vs. Reported Business Line Adds*



Source: Company reports, Merrill Lynch estimates.
* Net residential additions. Before TSR lines are subtracted.
RBOCs recover (in wholesale receipts) approximately 80% of revenues lost to CLECs using TSR.

What's Going On?

Data traffic continues to drive robust demand growth for the entire sector.

The IXCs, CLECs, independent telcos and the RBOCs continue to benefit from the explosive growth of Internet/data traffic as business customers are migrating from single POTs lines to higher-capacity DS-1s and from DS-1s to DS-3s to accommodate higher-capacity requirements. In addition, residential customers are adding second (in some cases third lines) for on-line connections.

The following three points summarize our views:

Business customers are migrating from POTs to high speed lines.

- As a result of the ballooning "need for speed," **we believe there is a migration of business customers trading up their single POTs lines for high-speed (as well as higher rate) data lines.** We estimate average high-speed data lines have grown 25-35% y/y with data revenues increasing 35-45%.

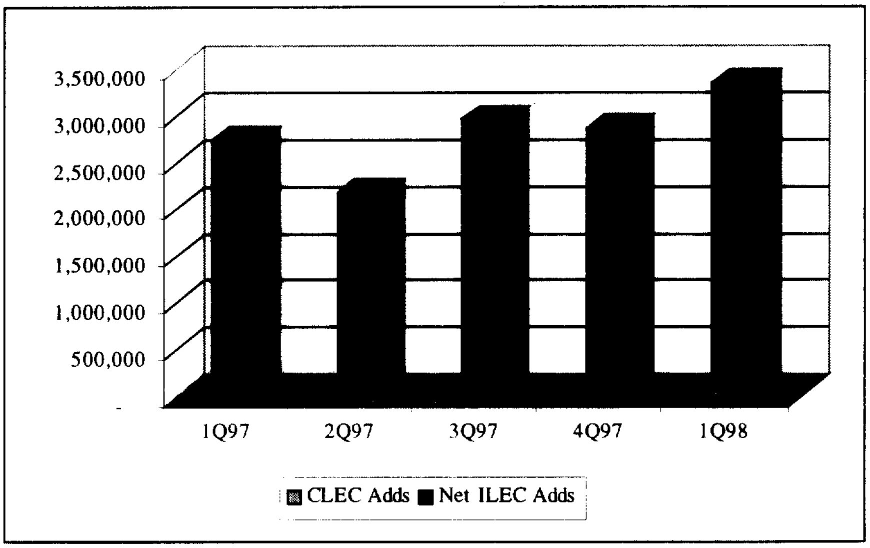
Traditional measure of line growth masks the real growth.

- Despite the slowdown in the RBOCs' reported switched business line additions in 1Q98, **our analysis suggests that the group's business line growth remains strong when high-speed lines, measured on an access line equivalent basis consistent with the CLECs, are included.** Traditional measures reported by the RBOCs do not reflect the business line migration phenomenon, because they only count single business (or POTs) lines.

The local pie continues to expand.

- **By including DS-1s and DS-3s in ILEC access line equivalent counts, we have not only captured the business line migration phenomenon, but also discovered the overall local telecom market is growing at a rate in which both newer entrants and the incumbents can benefit.** The CLECs continue to take share at a steady clip at the same time as the RBOCs and independent telcos have sustained line additions *(see Chart 4)*. The pie is getting bigger; thank you Internet, AOL, ISPs, fax machines, computer modems, etc.

Chart 4: Total U.S. Access Line Equivalent Adds



Assumes all CLEC adds are business lines.
Assumes Independents encompass 18% of ILEC business lines.
*ILEC line counts have been reduced to account for TSR lines which are normally double-counted.
Source: Company management, Merrill Lynch estimates

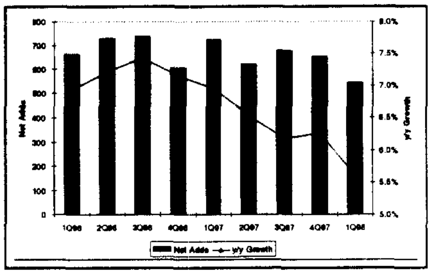
The RBOCs continue to benefit from their many sources of growth.

Although some traditional sources of growth for the RBOCs (e.g., single business lines, minutes and cellular) seem to be slowing, **new, non-traditional products/services continue to bolster the RBOCs top and bottom line growth rates.** We continue to expect a shift in the group's sources of growth as traditional telco products mature and new initiatives (e.g., PCS, data/Internet, advanced features such as voice mail and caller ID, international investments, security monitoring, high-speed lines, etc.) as well as continued efficiency gains expand.

Appendix: How the Numbers Are Reported

The reported numbers don't show all the growth.

Chart 5: Reported RBOC Business Line Growth & Quarterly Net Adds



Source: Company reports

Table 6: Reported RBOC Business Access Lines: The Wrong Way to Measure Lines*

	1Q96	2Q96	3Q96	4Q96	1Q97	2Q97	3Q97	4Q97	1Q98
Ameritech	6,326	6,433	6,542	6,629	6,751	6,817	6,929	7,098	7,183
y/y growth	*7.3%*	*7.0%*	*7.1%*	*6.8%*	*6.7%*	*6.0%*	*5.9%*	*7.1%*	*6.4%*
Net Adds	*119*	*107*	*109*	*87*	*122*	*66*	*112*	*169*	*85*
Bell Atlantic	12,644	12,886	13,096	13,287	13,488	13,700	13,926	14,111	14,298
y/y growth	*5.1%*	*5.9%*	*6.0%*	*5.7%*	*6.7%*	*6.3%*	*6.3%*	*6.2%*	*6.0%*
Net Adds	*75*	*242*	*210*	*191*	*201*	*212*	*226*	*185*	*187*
BellSouth	6,370	6,522	6,639	6,732	6,854	6,935	7,030	7,088	7,148
y/y growth	*7.9%*	*8.7%*	*8.5%*	*8.1%*	*7.6%*	*6.3%*	*5.9%*	*5.3%*	*4.3%*
Net Adds	*145*	*152*	*117*	*93*	*122*	*81*	*95*	*58*	*60*
SBC	10,711	10,919	11,132	11,307	11,509	11,714	11,918	12,092	12,263
y/y growth	*7.1%*	*7.6%*	*7.7%*	*7.5%*	*7.5%*	*7.3%*	*7.1%*	*6.9%*	*6.6%*
Net Adds	*195*	*208*	*213*	*175*	*202*	*205*	*204*	*174*	*171*
U S WEST	4,372	4,394	4,482	4,543	4,621	4,678	4,721	4,790	4,830
y/y growth	*7.0%*	*6.3%*	*7.3%*	*7.1%*	*5.7%*	*6.5%*	*5.3%*	*5.4%*	*4.5%*
Net Adds	*130*	*22*	*88*	*61*	*78*	*57*	*43*	*69*	*40*
Total Adds	**664**	**731**	**737**	**607**	**725**	**621**	**680**	**655**	**543**
Avg. y/y Growth	***6.9%***	***7.2%***	***7.4%***	***7.2%***	***6.9%***	***6.5%***	***6.2%***	***6.3%***	***5.6%***

* Wrong, because high-speed DS-1 and DS-3s are excluded
Source: Company reports

There are two important differences in the line count methodologies for the RBOCs and the CLECs:

The RBOCs do not include a majority of their high-speed lines in their reported access lines.

The first key distinction between the RBOCs' and the competitive local exchange carriers' (CLECs) access line figures is that the RBOCs exclude most of their high-speed lines while a majority of the CLECs count all of their high-speed connections in their total line tallies. In addition to the traditional POTs lines, only a portion of total ISDN lines are included in the RBOC line counts. As a result, the RBOCs' traditional way of measuring lines ignores the rapid growth of non-switched and high-speed data lines (i.e., a portion of the ISDNs, and all DS1s and DS3s). In contrast, most of the CLECs include all of their ISDN lines, DSOs, DS1s, and DS3s in their line counts. The following table shows how the RBOCs include ISDN lines in their access line counts (none include DS-1s or DS-3s):

Table 7: How ISDN Lines are Counted by the RBOCs

Company	Method Used in Equating ISDN Lines for Reported Access Line Counts
Ameritech	Count Primary Rate (PRI) ISDN lines and Basic Rate (BRI) ISDN Lines on a 1:1 basis.
Bell Atlantic	Count PRI ISDN lines as 23 line equivalents. Exclude BRIs.
BellSouth	BRI ISDN lines counted on a 1:1 basis. Exclude PRIs.
SBC	Actual PRI ISDN channels used is counted as 1 line equivalent (1-23 lines). Exclude BRIs.
US WEST	Only PRI ISDN line side channel termination is counted. Exclude BRIs.

Source: Company managements.